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Brian W. Masterson
Government Affairs Director

Suite 1000
1120 20th. St. NW
Washington, DC 20036
202 457-3803
FAX 202 457-2545
EMAIL bmasters@lgamgw.attm

December 18, 1998

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Magalie Rofman Salas, Secretary
Federal Communications Commission
445 Twelfth Street, SW Room TWB-204
Washington, D.C. 20554

Re: Notice of Ex Parte meeting: In the matter of Access Charge reform, CC
Docket No. 96-262; Price Cap Performance Review for LECs, CC Docket No.94-
1; MCI Telecommunication Corp. Emergency Petition for Prescription, CC
Docket No. 97-250; and Consumer Federation of America Petition for
Rulemaking, RM-9210.

Dear Ms. Salas:

On Thursday, December 17, 1998, Joel Lubin, Paul Malandrakis, and I met with Jane Jackson, Chief of the Competitive Pricing Division, Richard Lerner Deputy Chief of the Competitive Pricing Division, Doug Galbi, Jay Atkinson, Tamara Preiss, and Aaron Goldschmidt, from the Common Carrier Bureau of the Federal Communications Commission, concerning matters related to the referenced proceedings. We discussed the arguments reflected in AT&T's filings in these proceedings concerning access reform and LEC pricing flexibility. The written presentation used at the meeting is attached.

Two copies of this Notice are being submitted to the Secretary of the Commission in accordance with Section 1.1206(a)(2) of the Commission's rules.

Sincerely,

A handwritten signature in cursive script that reads "Brian W. Masterson".

Attachment

cc: Jane Jackson
Richard Lerner
Doug Galbi
Jay Atkinson
Tamara Preiss
Aaron Goldschmidt

*Access Charge Reform /
Price Cap Performance Review
for
Local Exchange Carriers*

*Update and Refresh the Record
October, 1998*

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Access Reform
Update and Refresh Record
October, 1998

AT&T's position....

- ~ The FCC's assumptions underlying its market-based approach are invalid and should be revisited.
- ~ Competition robust enough to drive down access rates has not developed anywhere in the nation, and the LECs continue to price at the upper limit in every basket.

Access Reform
Update and Refresh Record
October, 1998

AT&T's position continued....

- ~ Mechanisms should be adopted to reduce access charges to cost as soon as possible.
- ~ The FCC should accelerate the timetable on the prescriptive backstop to the market-based approach.
- ~ Access rates should be set at TELRIC.
- ~ In its price cap review, the FCC should increase the X-Factor to reflect interstate only data, rather than total company productivity data.

Access Reform
Update and Refresh Record
October, 1998

AT&T's position continued....

- ~ The FCC should *not* adopt the LECs' pricing flexibility proposals.
- ~ The FCC has already granted LECs considerable pricing flexibility
- ~ Without widespread competition, pricing flexibility will allow the LECs to act anticompetitively
- ~ The additional flexibility sought by the LECs is unwarranted
- ~ Customers oppose additional pricing flexibility for the LECs

The State of Local Competition

The State of Local Competition

According to MCI WorldCom:

- 1 year after the Commission adopted its Access Charge Reform Order & 2 years after the Local Competition Order, unbundled network elements (UNEs) are far from a “ubiquitous” substitute for access services.
- *Today the competitive landscape for interstate access charges has remained virtually unchanged.*
- Interstate access remains \$10B above forward-looking economic cost.

The State of Local Competition

According to MCI WorldCom:

- Of a total of 144.5 million access lines, only 123,680 have been sold to CLECs as unbundled elements.
- RBOCs and GTE are expected to add 6 million access lines between 1997 and 1998.
- ILECs continue to render UNE-based competition infeasible through prohibitively expensive non-recurring charges.

The State of Local Competition

According to MCI WorldCom:

Without local competition, there can be no exchange access competition, and the market-based approach will guarantee continued distortion of the market for long distance services, as well as excessive profits for the incumbent monopolists.

The State of Local Competition

According to Ad Hoc:

- Only 1% of the local service lines were being resold on a “bundled” (TSR) basis.
- Less than one tenth of one percent of local service lines were being provided over UNE loops purchased by CLECs.
- 0.14% of local numbers have been “ported” by ILECs to competing local service providers.

The State of Local Competition

According to Ad Hoc:

- Out of 11,500 serving wire centers only 420 (4%) had a physical collocation arrangement with at least one CLEC utilizing UNE loops.
- Only 367,921 or slightly over 1%, of the 32 million-plus access lines in the SBC region were identified as facilities-based CLEC services.

The State of Local Competition

According to Ad Hoc:

- ILECs switched 500 billion interstate access minutes in 1997, a 6.4% increase from 1996.
- There is no evidence that ILECs are suffering reduced use of switched access services due to competitive alternatives.

The State of Local Competition

According to Ad Hoc:

The Eighth Circuit ruling that ILECs need not recombine UNEs has created a severe technical impediment to CLECs ability to use UNEs efficiently and cost effectively.

The State of Local Competition

According to the Competition Policy Institute (CPI):

- It is now clear that consumers are not being served by market forces sufficient to bring down access charges.
- 8th Circuit rulings are ~~retarding~~ retarding the entry of new local exchange competitors using UNEs.

The State of Local Competition

According to the Competition Policy Institute (CPI):

- By the end of 1998, competitors to the ILECs will serve only about 1.4 million (0.8%) of the nation's estimated 177 million access lines through UNE based entry.

The State of Local Competition

According to the Consumer Federation of America(CFA), International Communications Association(ICA) & the National Retail Federation(NRF):

They petitioned the Commission to initiate a rulemaking addressing the immediate prescription of interstate access rates to cost-based levels because there is no meaningful level of competition and residential and business consumers are forced to pay bloated access charges.

- Ten months after the filing little has changed.

The State of Local Competition

According to CFA, ICA, & the NRF:

- There is total consensus among telecommunications customers regarding the lack of meaningful levels of competition.
- Leading financial analysts indicate that LECs “earnings growth is superior to the S&P 500”.

The State of Local Competition

According to Cable & Wireless USA, INC.:

- RBOCs have refused to provide reasonable collocation.
- Local competition continues to be thwarted by the RBOCs failure to implement operational support systems necessary to the use of UNEs.

The State of Local Competition

According to Cable & Wireless USA, INC.:

- Without a reasonable prospect of local competition in the near future, the primary assumption underlying the *Access Charge Reform Order* has proven incorrect.

The State of Local Competition

According to Cable & Wireless USA, INC.:

- As long as the local loop and switch remain bottleneck facilities, any carrier that controls those facilities will retain the incentive to keep its access charges as high as possible.

The State of Local Competition

According to SPRINT:

- There are no appreciable cost savings to SPRINT in using alternative vendors, which lessens their ability to exert effective pressure on ILEC access charges.
- Some CLECs are seeking to charge 12 times the access rate charged by ILECs, as a source of funding their start-up costs.

The State of Local Competition

- *According to SPRINT:*
- Because of the failure of competition to have the desired effects on switched access charges, the Commission should follow a prescriptive approach.
- The Commission should order ILECs to file forward-looking studies now, rather than waiting until 2001.

THE X-FACTOR SHOULD BE INCREASED TO
REFLECT THE HIGHER PRODUCTIVITY
GROWTH OF INTERSTATE ACCESS SERVICES.

There is no credible evidence that the X-Factor has declined in recent years, as the LECs contend.

On the surface, USTA's update of the FCC's productivity study appears to show a declining X-Factor.

These results, however, cannot be blindly accepted at face value without examining the components of the X-factor and understanding the underlying factors at work.

ADJUSTMENTS TO THE USTA STUDY

Estimated X-Factors

| | 1996 | 1997 | 1987-97 |
|---------------------------|-------|-------|---------|
| Total Company Estimates | | | |
| Gollop Study | 2.1% | 4.1% | 5.4% |
| Use published data | 2.5% | 5.2% | 5.5% |
| Use local DEMs | 5.2% | 9.7% | 6.2% |
| Adjust for LEC earnings | 9.0% | 8.5% | 6.4% |
| Adjust for access reform | 8.9% | 8.5% | 6.2% |
| Interstate-only Estimates | | | |
| Use interstate output | 6.6% | 10.0% | 10.0% |
| Adjust for separations | 8.0% | 9.9% | 10.4% |
| Adjust for LEC earnings | 11.8% | 8.8% | 10.7% |
| Adjust for access reform* | 11.3% | 8.5% | 9.8% |

* According to Gollop's estimates, access reform reduces interstate output growth and the X-Factor by 0.51% in 1996, 0.29% in 1997, and 0.89% for the entire 1987-97 period.

INDUSTRY CONTRIBUTION ANALYSIS -- Non-Rural Only

| TABLE 2: Contribution from Interstate Switched Access | | | | | |
|---|---|----------------------------|----------------|--------------------------|--------------------------------------|
| Company | 1998 Total Switched AMOU (Millions) | Switched Access per Minute | | Contribution from Access | |
| | | Economic Cost* | ILEC Rates** | Per Access Minute*** | Annualized Total (\$ Millions)*** |
| | | (Blended Hatfield) | (as of 7/1/98) | | |
| Ameritech | 54,348 | 0.00224 | 0.0167 | 0.0145 | 786 |
| Bell Atlantic | 74,686 | 0.00257 | 0.0142 | 0.0116 | 869 |
| NYNEX | 58,884 | 0.00209 | 0.0249 | 0.0228 | 1,343 |
| Bell South | 80,671 | 0.00238 | 0.0199 | 0.0175 | 1,413 |
| PacTel | 42,652 | 0.00235 | 0.0146 | 0.0123 | 522 |
| SBC | 45,684 | 0.00265 | 0.0168 | 0.0142 | 646 |
| USWest | 60,089 | 0.00286 | 0.0220 | 0.0191 | 1,150 |
| Sub-Total RBOCs | 417,014 | 0.00245 | 0.0186 | 0.0161 | 6,730 |
| GTE | 52,855 | 0.00546 | 0.0293 | 0.0238 | 1,260 |
| SPRINT | 22,707 | 0.00517 | 0.0240 | 0.0188 | 428 |
| Cincinnati | 3,128 | 0.00413 | 0.0161 | 0.0120 | 37 |
| Lincoln | 727 | 0.00939 | 0.0228 | 0.0134 | 10 |
| Rochester | 2,521 | 0.00507 | 0.0235 | 0.0184 | 46 |
| SNET | 8,814 | 0.00284 | 0.0194 | 0.0166 | 146 |
| Other Non-Rural | 2,752 | 0.00718 | 0.0282 | 0.0210 | 58 |
| Total Non-Rural | 510,518 | 0.00295 | 0.0200 | 0.0171 | 8,715 |
| Less USF Flowback | | | | | 852 |
| Total Non-Rural Contribution -- adjusted for USF Flowback | | | | | 7,863 |

Notes: * Hatfield Default Scenario (80% Dedicated and 20% Tandem)

** Switched Access Unit Cost includes PICC Common Line, which is approximately 18% of the cost

*** Includes USF FLOWBACK of \$852 millions which is on an average 9.78% of the contribution.